

Internal Revenue Service

memorandum

TL-N-6390-88

CC:TL:TS/MAKEYES

date: **JUL 26 1988**

to: Deputy Regional Counsel (TL), Midwest Region CC:MW
Attention: Harmon Dow

from: Director, Tax Litigation Division CC:TL

subject: Post Review of Advisory Opinion on Statute of Limitations
[REDACTED]

This memorandum is in response to your May 10, 1988, request for post review of an advisory opinion issued by your region on April 14, 1988. The advisory opinion dealt with the effect of piggyback agreements on the statute of limitations.

ISSUE

1. Whether the assessment of any deficiency due for the [REDACTED] year is barred by the statute of limitations, if a piggyback agreement is executed by the Service and taxpayer, after the normal period of limitations has expired, even though the piggyback agreement extends the statute of limitations for two years after the decision in the controlling case becomes final?

FACTS

Taxpayers timely filed a 1040 return for the [REDACTED] year which reported a loss on their Schedule C for the [REDACTED] computer leasing project. No consents were executed to extend the statute of limitations on assessment for the [REDACTED] year. The normal period of limitations for the [REDACTED] year expired on [REDACTED]. Taxpayers did file a protective claim for the [REDACTED] year on [REDACTED], pending the outcome of the [REDACTED] litigation. The Service Center acknowledged receipt of the protective claim and indicated that the claim would be forwarded to the local Examination Division. As a result, Fargo District offered to the taxpayers, on [REDACTED], a piggyback agreement tying the [REDACTED], [REDACTED], and [REDACTED] years to a docketed [REDACTED] test case. The taxpayers executed the piggyback agreement on [REDACTED] which purported to extend the statute of limitations for two years following the final decision in the [REDACTED] controlling case.

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CONCLUSION

We disagree with the conclusion that the statute of limitations has been "waived" 1/ for the [REDACTED] year. The [REDACTED] year was barred at the time the piggyback agreement was entered into by the taxpayers and the Service. According to the facts, there had been no extension of the statute of limitations prior to the execution of the piggyback agreement. Therefore, the piggyback agreement could not extend the statute of limitations for the [REDACTED] year, although it was effective to extend the period of limitations for the [REDACTED] and [REDACTED] years. The filing of a protective claim does not extend the statute of limitations on assessment.

DISCUSSION

A closing agreement can not be used to obtain an extension of the statute of limitations when the statutory period has already expired. Section 6501(a) provides a three year period of limitations for assessment. This three year period can be extended by agreement pursuant to section 6501(c)(4). That section provides:

Extension by Agreement-Where, before the expiration of the time prescribed in this section for the assessment of any tax imposed by this title, except the estate tax provided in Chapter 11, both the Secretary and the taxpayer have consented in writing to its assessment after such time, the tax may be assessed at any time prior to the expiration of the period agreed upon. The period so agreed upon may be extended by subsequent agreements in writing made before the expiration of the period previously agreed upon. [Emphasis supplied].

The plain language of section 6501(c)(4) makes it clear that the period of limitations can not be extended by a consent, unless the consent is executed prior to the expiration of the period of limitations. Therefore, any agreement to extend the statute of limitations once it has already expired is unenforceable.

1/ The statute of limitations on assessment is extended by consent. Restrictions on assessment under section 6213(d) are "waived."

We agree that a closing agreement can be used to extend the statute of limitations on assessment. However, the closing agreement must be executed prior to the expiration of the normal period of limitations. We do not agree in this case that paragraph 4 of the piggyback agreement extended the statute of limitations for the [REDACTED] year. Paragraph 4 provided that:

Any tax or additions to tax (plus statutory interest) attributable to the Tax Shelter adjustment may be assessed by the IRS any time within two (2) years after the date on which the decision in the controlling case becomes final, notwithstanding the expiration of any period of limitation on assessment and collection otherwise prescribed by section 6501.

Normally, the Service would have 60 days to make assessments after the decision becomes final. See section 6501(a). Paragraph 4 allows the Service two years to assess once the decision becomes final, instead of the normal 60 days to assess. However, it does not extend the statute for assessment unless the agreement is executed while the statute of limitations is open. Since the statute of limitations for assessment had expired prior to execution of the agreement, the period of limitations was not extended.

Furthermore, the filing of the protective claim by the taxpayers on the last day to extend the statute of limitations for assessment does not extend the statute of limitations for assessment. The filing of the protective claim will however, protect the statute for filing a refund suit. Since you indicated that no agreement was executed to extend the statute of limitations on assessment for the [REDACTED] year, the Service will be barred from assessing for that year. However, if a refund suit is filed, the Service will be entitled to offset up to the amount of the refund, that which might have been properly assessed and demanded. See Lewis v. Reynolds, 284 U.S. 281 (1932).

It is the Service's position that any amount assessed or collected after the expiration of the period of limitations is an "overpayment", pursuant to section 6401, and subject to refund or abatement under section 6402(a), if the taxpayer files a timely claim for refund in accordance with section 6511(a). See Rev. Rul. 74-580, 1974-2 C.B. 400. Compare that situation with the situation in Rev. Rul. 85-67, where the taxes and interest were paid before the expiration of the statute of limitations on assessment, but no assessment occurred prior to the expiration of the statute of limitations under section 6501(a). In that situation, it is the Service's position that the payment is not an overpayment within the meaning of section 6401(a) and is not refundable even though it has not been assessed. See Rev. Rul. 85-67, 1985-1 C.B. 364. In this case, if there has been no

payment made by taxpayers prior to the expiration of the statute of limitations on assessment, then any amounts later collected are subject to refund, provided a timely claim for refund is made. See section 6511(a).

Over the years the Service's and the Courts' position on overpayments and the effect of a consent on the statute of limitations for assessment has been inconsistent. 2/ To date, there has never been any judicial resolution on the issue of the effect of a closing agreement, signed after the statute of

2/ Part of the reason for the inconsistent positions had to do with the code being amended and the way the courts have interpreted the issue. Prior to 1928, consent agreements extending the statute of limitations could be executed at any time. The Revenue Act of 1928 enacted section 506(a), which amended section 278(c) so that consent agreements had to be executed prior to the expiration of the period of limitations. The 1928 Act also repealed section 1106(a) and enacted section 607 and 608 (sections dealing with the effect of the expiration of the statute of limitations on assessment and collection). Section 607 was intended to clear up some of the doubts created by section 1106(a) of the 1926 Act concerning the effect of voluntary and involuntary payments.

The question which was raised by section 607 was whether the bar of section 6501(a) bars the remedy of collection or extinguishes the liability for the tax. In Horuff v. United States, 9 F.Supp. 1016 (Ct. Cl. 1935), the Court came to the conclusion that an amended return was a valid waiver of the period of limitations. Therefore, there was no overpayment. The Court went on to infer that there was a common law method to waive the statute of limitations. Although Horuff was decided after the Code had been amended to require a consent be executed prior to the expiration of the statute of limitations, there was an exception for consents executed prior to January 1929. Horuff's facts fell under that exception and there was support for the conclusion that the statute had been extended. However, in Elmer M. Melahn, 9 T.C. 769 (1947), the Tax Court in a reviewed decision held that the only method by which a taxpayer could extend the statute of limitations was provided in the code (section 276(b) of 1939 code). The Court specifically noted that a different result would have been reached in Horuff had section 276(b) of the 1939 code been applicable. The Court held that the extension of the statute of limitations after it had expired was ineffective. The next case in which the issue was considered was Diamond Gardner Corp., 38 T.C. 875 (1962), which is the Service's position today and is discussed in more detail in this memorandum.

limitations had expired and for which voluntary payment was made or for which collection had been attempted. However, there has been litigation where the Service has tried to assert a deficiency after the statute of limitations had expired .

In Diamond Gardner Corporation, Transferee v. Commissioner, 38 T.C. 875, 879-881 (1962), the Tax Court held that the effect of the statute of limitations for assessment is "for all practical purposes to extinguish a barred tax liability." The Court also held "any payment by a taxpayer of a barred tax liability, whether voluntary or involuntarily, automatically becomes an 'overpayment' and hence subject to mandatory refund." The Court went through the legislative history of the effect to be given the bar of the statute of limitations on assessment. Section 1106(a) of the Revenue Act of 1926, as well as section 607 of the Revenue Act of 1928 (predecessor of current section 6401(a)) were thoroughly discussed and were the basis of the Court's conclusion. The Senate Report for the Revenue Act of 1928, in discussing section 607, noted that it was immaterial whether the payment was voluntary or involuntary and duress was of no significance in determining the right to recover an amount paid after the statute has expired. See S. Rep. No. 960, 70th Cong., 1st Sess. (1928), C.B. 1939-1 (Part 2), 437-438.

The Service however, in G.C.M. 33176, Assessment of Tax and Interest on Amended Returns Filed After Expiration of Normal 3-Year Assessment Period, I-1295 (Jan. 20, 1966) took a different position from the Tax Court regarding whether voluntary payments made after the statute of limitations had expired were subject to mandatory refunds. The thinking was, if a taxpayer voluntarily submitted payment, and amended his return after the statute of limitations had expired, the taxpayer had waived the bar of the statute of limitations and therefore no overpayment was made. G.C.M. 33176 relied upon Horuff v. United States, 9 F.Supp. 1016 (Ct. Cl. 1935). The Service rejected Melahn and Diamond Gardner, *supra*, as controlling on the issue. Those cases dealt with proceedings initiated by the Service and not with a taxpayer voluntarily reviving a tax liability.

The foregoing G.C.M. was revoked by G.C.M. 34790, In re: [REDACTED] (Feb. 23, 1972). In that G.C.M., the Service came to the conclusion that voluntary payments accompanying amended returns, filed after the expiration of the statute of limitations on assessment or collection did not operate as an extension of the statute. Furthermore, the G.C.M. concluded that such voluntary payments constituted overpayments under section 6401(a) which should be refunded under section 6402 (a), if the taxpayers make a timely claim for refund under section 6511(a). The Service also acknowledged the Tax Court precedent (Melahn and Diamond Gardner) as controlling on the issue.

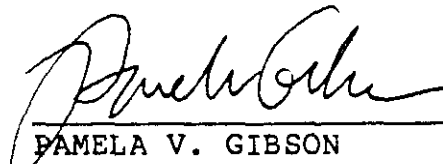
In G.C.M. 33699, In re: Closing Agreements, I-2139 (Dec. 5, 1967), it was stated that the net effect of the code sections, case law, and Chief Counsel memoranda indicated that the Service should not use closing agreements for years that have been barred by the statute of limitations and any payments made after the statute had expired were subject to refund.

For the reasons stated in this memorandum, no assessment should be made for the [REDACTED] year. It has been barred by the statute of limitations. However, from the information you have made available, it appears that the statute of limitations was extended for the [REDACTED] and [REDACTED] years.

Should you have any questions regarding this memorandum, please contact Marsha Keyes at FTS 566-4174.

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